AR-0142

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

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UNITED STATES OF AMERICA,

Plaintiff,

- against -

CHANCELLOR MEDIA COMPANY, INC.,
and
SFX BROADCASTING, INC.,

Defendants.

--X

Civil Action
No. CV-97-6497

Filed: November 6, 1997

Complaint

The United States of America, acting under the direction of the Attorney General of the United States, brings this civil antitrust action to prevent the proposed acquisition by Chancellor Media Company, Inc. (Chancellor) of certain radio stations from SFX Broadcasting, Inc. (SFX).

I. Nature of the Action

1. The proposed acquisition will combine under one owner the leading radio stations on Long Island. As Chancellor's chief financial officer told the board of directors, the acquisition "will make Chancellor the dominant radio broadcaster" on Long Island.

2. Chancellor and SFX are the number one and number two radio companies on Long Island. The three key stations owned by Chancellor (WALK-FM) and SFX (WBLI-FM and WBAB-FM) frequently garner the highest ratings in the demographic groups most important to Suffolk County advertisers. These two companies generate the highest advertising revenues among Long Island radio stations. By Chancellor's own account, "WALK, WBLI and WBAB combined own about 63% of a market with 36 million in net revenues."

3. WALK-FM (Chancellor) and WBLI-FM/WBAB-FM (SFX) have been locked in daily battle against each other for listeners and for advertising revenues. Suffolk County advertisers over the years have played the Chancellor and SFX stations off against each other to get lower advertising rates and better promotional services. WALK's Director of Sales wrote that WALK was "[f]ighting WBLI['s] and WBAB['s] low 'firesale' rates." The competition between these stations has been an essential element in keeping down prices for Suffolk County radio advertising. The acquisition would end this battle ; in Chancellor's own words describing the acquisition: "The War is Won."

4. The company officials who would operate the stations believe that the acquisition "will result in less competitive 'undercutting'" and that "[r]ates will increase as a result of removal of competitive pressures." Eliminating competition between WALK and WBLI/WBAB will increase radio advertising prices and diminish the quality of promotional services. The combination will harm many

local businesses that rely on Suffolk County radio as an efficient and effective way to tell their customers about their products and services.

II. Defendants

5. Chancellor is a Delaware corporation headquartered in Irving, Texas. It is the second largest radio broadcaster in the United States and currently owns 95 radio stations in 21 major U.S. markets, including a presence in each of the 12 largest markets. Chancellor is a recent conglomeration of Evergreen Media Corp., Chancellor Broadcasting Company and Viacom International, Inc.'s former radio group. The Chancellor stations generate annual revenues in excess of $800 million. Chancellor's revenues in 1996 from WALK-FM and WALK-AM in Suffolk County, Long Island were $13.3. million.

6. Chancellor's largest and controlling shareholder is the investment partnership of Hicks, Muse, Tate & Furst (Hicks Muse). Hicks Muse owns approximately 18 percent of Chancellor. Hicks Muse also wholly owns Capstar Broadcasting Partners (Capstar). Capstar operates 225 stations in 70 markets.

7. SFX is a Delaware corporation headquartered in New York, New York. SFX owns or operates 85 radio stations located in 23 markets in the United States, including the following four stations on Long Island: WBLI-FM, WBAB-FM, WHFM-FM, and WGBB-AM. SFX's revenues in 1996 were approximately $282 million, about $11 million of which were derived from sales by its Long Island-based radio stations.

III. The Proposed Acquisition

8. On or about July 1, 1996, Chancellor and SFX entered into an asset exchange agreement whereby SFX agreed to exchange its four Long Island-based radio stations for Chancellor's two Jacksonville, Florida radio stations and an additional $11 million. The total value of the Long Island portion of the acquisition is approximately $54 million.

9. Prior to the July 1, 1996 agreement, Chancellor and SFX stations on Long Island were vigorous competitors of each other. When the asset exchange agreement was entered, however, Chancellor began operating SFX's stations pursuant to a Local Marketing Agreement (LMA). An LMA is an agreement to take operating control of a station before taking ownership. The LMA includes the right to sell advertising time and to program the station.

10. On or about August 24, 1997, Hicks Muse entered into an agreement to acquire all of SFX, including SFX's Long Island stations. This acquisition has not yet been consummated, and is under investigation by the Department of Justice.

IV. The proposed acquisition is likely to reduce competition substantially for radio advertising time for coverage of Suffolk County in violation of the Clayton and Sherman Acts

A. How customers benefit from competition among radio stations

11. The defendants' radio stations, like most commercial radio stations, generate almost all their revenues from the sale of advertising time, In general,

radio stations attract listeners, and then sell access to those listeners (that is, advertising time) to businesses who want to advertise their products. Radio stations compete among themselves to attract advertisers by programming their stations to attract listeners, especially in particular demographic groups. A demographic group is a way of describing the listeners by such characteristics as age and sex. Radio stations then offer advertisers access to their listeners at prices that reflect their listenership levels (ratings) in the demographic groups that advertisers are attempting to reach.

12. Radio stations price their advertising time in large part on the basis of the number of listeners that they reach. Traditionally, this is expressed on a cost-per-thousand (CPM) basis. When buying radio advertising time, advertisers consider the CPM and the overlap of the number and demographic characteristics of a radio station's listeners with the advertisers' likely customers.

13. Advertisers often are interested in reaching particular demographic groups, because they believe the groups are their likely customers. Advertisers prefer to purchase access to listeners who are their likely customers, and not to waste money by paying to advertise to listeners who are unlikely to purchase their products.

14. If a station individually or number of stations in combination efficiently reach an advertiser's target demographic group, the advertiser has a choice in how to reach its potential customers. This choice creates competition between radio stations and results in lower prices and better services.

B. Competition between Chancellor and SFX has benefited customers who want to reach Suffolk county listeners

15. The defendants' radio stations competed to serve a single distinct geographic area--Suffolk County. Although WALK's and WBLI's signals effectively cover most of Long Island, most of their listeners reside in Suffolk County. In the key "adults aged 25-54" demographic group, Suffolk County listeners comprise about 95 percent of WALK's and WBLI's total listeners, and about 75 percent of WBAB's total listeners. These stations, unlike those New York City radio stations whose signals penetrate at least partly into Suffolk County, consciously seek to promote themselves as stations that serve Long Island.

16. When the Chancellor and SFX stations operated independently, they were good substitutes for each other. The stations competed head-to-head to reach adults aged 25-54, and consistently were three of the four top-rated stations among Suffolk County listeners in this important listener demographic. Many local and regional advertisers seeking to reach Suffolk County listeners aged 25-54 could reach this audience efficiently by purchasing time on Chancellor or SFX stations or by using a combination of Chancellor, SFX and other stations in the market, such as those owned by the Barnstable Broadcasting, Inc. (Barnstable) group. However the Barnstable stations, either alone or in combination with other stations, have not offered a sufficient number of listeners in this demographic group to be an effective substitute for Chancellor or SFX stations.

17. When the Chancellor and SFX stations operated independently, advertisers could obtain lower prices by “playing off” Chancellor-owned stations against SFX stations. Advertisers used the threat to move their business between the Chancellor and the SFX stations to get more favorable prices and services at each. Advertisers in Suffolk County paid less for advertising as a result of price competition between the Chancellor and SFX radio stations.

C. The proposed acquisition will allow Chancellor single-handedly to raise prices to many advertisers

18. Chancellor’s acquisition of the SFX stations would eliminate the competitive alternative that has resulted in lower prices for advertising to Suffolk County radio listeners. As a consequence, Chancellor will have the ability to raise price to many advertisers -- especially local and regional advertisers.

19. Price increases made possible by the acquisition are likely to be profitable. This is because Chancellor will be able to raise price selectively without losing a significant amount of business. Radio stations know a great deal about how likely an advertiser is to turn to an alternative. In the negotiation process, for example, radio stations obtain significant information about an advertiser’s objectives. As a result, radio stations know that some advertisers are more likely than others to turn to alternatives. Because prices are set through individual negotiation, stations can charge higher prices to advertisers that are less likely to use alternatives, while charging lower prices to those advertisers that would more readily switch. Consequently, Chancellor will be able to raise price profitably to the

many advertisers that would readily switch between Chancellor and SFX long before they would consider other alternatives.

1. Many advertisers lack good alternatives to the Chancellor/SFX stations

a. Advertisers could not turn to other Suffolk County radio stations to prevent Chancellor from imposing an anticompetitive price increase

20. Barnstable is the only company other than Chancellor and SFX that generates more than five percent of the total radio revenues spent by advertisers on Long Island-based radio stations that offer coverage of Suffolk County ("Suffolk County stations"). Barnstable owns WBZO-FM, the only other Suffolk County station that generates ratings and advertising revenues that come close to those of WBLI or WBAB. It is significantly smaller than WALK. However, WBZO would not be able to offer, individually or in combination with any non-Chancellor stations, enough listeners in the Chancellor/SFX-dominated demographics to provide a non-Chancellor alternative for many advertisers who want access to Suffolk County radio listeners. Moreover, Barnstable cannot significantly increase its attractiveness to customers simply by lowering its prices, because it does not offer what the customers want in terms of listeners. Consequently, WBZO is unlikely to constrain significantly the ability of Chancellor to raise prices. Indeed, a Chancellor price increase may provide an opportunity for Barnstable to increase its prices.

21. There are a number of other radio broadcasters on Long Island, but their stations attract very small ratings and small amounts of radio advertising compared to the Chancellor and SFX stations. Individually or in combination, they are less able than Barnstable to offer an alternative for those advertisers -- especially local and regional advertisers -- who would have to deal with Chancellor to gain access to Suffolk County radio listeners after the proposed acquisition.

b. Entry of new Suffolk County radio stations is unlikely to prevent Chancellor from imposing an anticompetitive price increase

22. In projecting the effect of the acquisition, WALK's General Sales Manager wrote that Long Island:

> is a market with great potential *and a relatively easy one to consolidate*. 63% of the region's radio revenues come from 3 stations-WALK, WBLI and WBAB. [Emphasis added]

23. WALK's General Sales Manager's statement expressly notes that the market has only a few competitors, and implies that no other station, existing or new, is likely to threaten the position of those competitors. Most of the remaining broadcasters are handicapped by their limited signal coverage and could not develop into significant competitors. In addition, there is likely to be no opportunity for meaningful new entry into this market that would deter Chancellor's post-acquisition exercise of market power.

24. Except for WBZO, all other Long Island-based radio stations have low ratings and revenues. These stations do not and would not in the foreseeable future

constrain any anticompetitive price increases imposed by the combined Chancellor/SFX stations.

25. All but one of the other Suffolk County FM stations are weaker signals that are located in the more sparsely populated eastern end of Suffolk County; they cannot be heard in the heavily populated portions of Suffolk County. The AM stations heard in Suffolk County are also weak and, more generally, do not match FM sound quality. These stations could not attract many listeners -- no matter how good their programming is or becomes -- given their limited geographic reach and signal quality. FCC regulations prohibit these stations from significantly expanding their signal coverage.

26. In any event, it is difficult and time-consuming for stations with low ratings to expand their ratings significantly. Stations that are not performing well with their current formats are unlikely suddenly to become attractive to listeners because of a merger. Furthermore, attempting to expand listenership by radically reformatting is financially risky. According to Chancellor's General Manager for the Long Island stations, significant reformatting is the equivalent of "blow[ing]... up" your station. A broadcaster is unlikely to take such a risk simply to capitalize on a small but significant price increase by the Chancellor stations.

27. There is no available spectrum to add other high power FM signals on Long Island. There also is no available spectrum to add other low power FM signals in the more densely populated parts of Suffolk County. Although there is room in the spectrum to add new low power FM frequencies on the eastern end of

Suffolk County, these stations would lack the signal coverage to penetrate into the population centers of Suffolk County, and therefore would lack the ability within two years to develop listenerships that would rival those enjoyed by WALK, WBAB and WBLI.

28. Meaningful entry would not be likely, timely or sufficient to undermine an anticompetitive price increase.

c. Non-Long Island-based radio stations could not prevent Chancellor from imposing anticompetitive pricing on many advertisers

29. There are some Long Island-based radio stations that cover Nassau County, but do not generate significant listenership in Suffolk County. Advertisers (especially local and regional advertisers) who desire significant coverage of Suffolk County do not consider these Nassau County radio stations to be cost-effective substitutes for defendants' Suffolk County radio stations.

30. There are a few New York City radio stations that generate significant listenership in Suffolk County. These radio stations also broadcast throughout the New York tri-state metropolitan area, and have numerous listeners in Nassau County, the five boroughs of New York City, Westchester County, and parts of New Jersey and Connecticut. An advertiser pays to reach the entire tri-state New York metropolitan radio market when buying advertising time on a strong New York City radio station. Therefore, advertising prices on these stations are at least twice as expensive, per-Suffolk County listener, as prices on a Suffolk County station.

31. Non-Long Island radio stations do not provide cost-effective access to Suffolk County customers for many local advertisers. These advertisers do not want to “waste” their advertising dollars on listeners in other parts of the New York tri-state metropolitan area who are unlikely to be their customers. Some regional advertisers also would not find it cost-effective to substitute non-Long Island radio stations for Suffolk County radio stations.

32. Many advertisers would not turn to radio station alternatives located outside of Long Island in response to a small but significant increase in radio advertising prices charged by Suffolk County stations. Because Suffolk County stations would be able to charge higher prices to these customers without losing the business of other advertisers, a small but significant price increase would be profitable.

33. Suffolk County, Long Island is a relevant geographic market within which to assess the competitive effects of the proposed acquisition.

d. Other media will not constrain Chancellor’s ability to raise price to many advertisers

34. Radio stations see other radio stations as their principal competition. For example, in 1991, WBAB noted that “pressure from other [radio] stations keep [sic] us from selling new business at the rates we want to get.” In its 1996 Sales Budget Report the head of WBLI and WBAB sales lamented to the General Manager that “WALK and WBZO are the primary barriers to increasing rate[s].”

35. For many advertisers, other media do not serve as substitutes for radio advertising. Radio enjoys unique access to certain audiences. A radio is portable; people can listen to radio anywhere especially in places and situations where other media are not present, such as in the car. In addition, radio formats can target listeners in specific demographics. These features make it a more effective means for many advertisers to achieve what the advertising industry refers to as "frequency."

36. Many advertisers who purchase time on Suffolk County stations consider such purchases preferable to purchase of other media to meet their specific needs. When these advertisers use radio as part of a "media mix," they often view the other advertising media (such as television or newspapers) as a complement to, and not a substitute for, radio advertising.

37. Radio stations also provide certain value-added services or promotional opportunities -- such as contests, disc jockey endorsements, live remote broadcasts and greater flexibility in ad placement -- that many advertisers significantly value, and which many advertisers cannot exploit as effectively using other media.

38. For many advertisers, radio advertising is more cost effective than other media, like television and newspapers, in reaching their likely customers.

39. Many advertisers who use radio as part of a multi-media campaign do so because they believe that the radio component enhances the effectiveness of their overall advertising campaign.

40. Many advertisers, especially local and regional advertisers, would not switch their radio advertising purchases to other media if radio prices rose a small but significant amount in relation to other media prices. Because Suffolk County stations would be able to charge higher prices to these customers without losing the business of other advertisers, a small but significant price increase would be profitable.

41. The relevant product market within which to assess the competitive effects of this proposed acquisition is the sale of radio advertising time.

2. The effect of the acquisition would be substantially to lessen competition in the relevant market

42. The provision of radio advertising time for coverage of Suffolk County is a relevant market (*i.e.*, a line of commerce and a section of the country) within the meaning of Section 7 of the Clayton Act, 15 U.S.C. § 18.

43. The proposed acquisition and the LMA would have the following effects, among others:

1. competition in the sale of radio advertising time for coverage of Suffolk County would be substantially lessened;

2. actual and potential competition between Chancellor and SFX radio stations in the sale of advertising time -- especially to regional and local advertisers -- would be eliminated;

3. Chancellor's shares of the relevant market will increase from 33 percent to over 65 percent, whether measured by radio advertising revenues or by listenership. Using a measure of market concentration called the Herfindahl-Hirschman Index ("HHI"), explained in Appendix A, the acquisition would yield a

post-merger HHI of at least 4975, representing an increase of 2085; and

4. prices for radio advertising for coverage of Suffolk County would likely increase, and the quality of promotional services would likely decline -- especially to regional and local customers.

44. The proposed acquisition by Chancellor is likely to lessen competition substantially in interstate trade and commerce, in violation of Section 7 of the Clayton Act, and the LMA unreasonably will restrain interstate trade and commerce, in violation of Section 1 of the Sherman Act.

V. Jurisdiction and Venue

45. This action is filed pursuant to Section 15 of the Clayton Act, as amended, 15 U.S.C. § 25, and Section 4 of the Sherman Act, 15 U.S.C. § 4, to obtain equitable relief to prevent a violation of Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18, and Section 1 of the Sherman Act, as amended, 15 U.S.C. § 1.

46. Both Chancellor and SFX sell radio advertising time in this District. The sale of radio advertising time is a commercial activity that substantially affects, and is in the flow of, interstate trade and commerce. The defendants purchase substantial quantities of equipment, services, and supplies from sources located outside of New York. They also acquire funding for their New York radio operations from outside of New York. The Court has jurisdiction over the subject matter of this action and jurisdiction over the parties pursuant to 15 U.S.C. §§ 4, 22, and 25, and 28 U.S.C. §§ 1331 and 1337.

47. Venue in this District is proper under 15 U.S.C. § 22 and 28 U.S.C. § 1391(c).

VI. Requested Relief

48. The plaintiff requests: (a) adjudication that Chancellor's proposed acquisition would violate Section 7 of the Clayton Act and Section 1 of the Sherman Act; (b) permanent injunctive relief preventing the consummation of the proposed acquisition; (c) a finding that the LMA between Chancellor and SFX regarding SFX's Suffolk County radio stations violates Section 1 of the Sherman Act and termination of the LMA within 30 days after the Court's Order permanently enjoining the proposed acquisition; (d) an award to the United States of the costs of this action; and (e) such other relief as is proper.

Dated: November 6, 1997

_________/s/___________
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APPENDIX A
HERFINDAHL-HIRSCHMAN INDEX CALCULATIONS

"HHI" means the Herfindahl-Hirschman Index, a commonly accepted measure of market concentration. It is calculated by squaring the market share of each firm competing in the market and then summing the resulting numbers. For example, for a market consisting of four firms with shares of thirty, thirty, twenty, and twenty percent, the HHI is 2600 ($30^2 + 30^2 + 20^2 + 20^2 = 2600$). The HHI takes into account the relative size and distribution of the firms in a market and approaches zero when a market consists of a large number of firms of relatively equal size. The HHI increases both as the number of firms in the market decreases and as the disparity in size between those firms increases.

Markets in which the HHI is between 1000 and 1800 points are considered to be moderately concentrated, and those in which the HHI is in excess of 1800 points are considered to be concentrated. Transactions that increase the HHI by more than 100 points in concentrated markets presumptively raise antitrust concerns under the Horizontal Merger Guidelines issued by the U.S. Department of Justice and the Federal Trade Commission. See *Merger Guidelines § 1.51.*